

On the form and
presentation
of the government
of manitoba's budget

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ON THE FORM AND PRESENTATION OF THE GOVERNMENT OF MANITOBA'S BUDGET
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Let us define the "Budget" of the Government of Manitoba as a group of related documents which describe the financial condition of the Province. These include (1) the Estimates of Revenue and Expenditure for the coming fiscal year (in earlier years separate estimates were presented for capital expenditures), (2) the Budget Speech which presents the estimates in summary form and describes any tax or other revenue changes that are being proposed, (3) the Public Accounts, which present detailed information on revenues, expenditures, financial assets and liabilities and on the source and application of funds for the fiscal year just completed and (4) the Auditor's Report which evaluates and criticizes the way in which the Province handles and reports upon its financial affairs. In addition, in recent years the Province has issued a quarterly report which provides information on revenues and expenditures since the beginning of the fiscal year and gives revised estimates for the balance of the fiscal year. It also issues a Financial Report which presents the principal information from the Public Accounts in summary form. While this report concentrates its attention in the main on the budgetary presentation of revenues and expenditures, in some degree it is also concerned with the entire set of documents.

While the main emphasis of the report is on the Government's Budget, it must be recognized that a government's financial operations have traditionally been divided between the budgetary and non-budgetary. According to one definition, non-budgetary items are those which do not enter the calculation of the annual budgetary deficit or surplus but which may increase or decrease government assets and liabilities. To provide a complete picture of the Government's financial condition, some attention will be paid to non-budgetary items as well.

In large measure, this difference between budgetary and non-budgetary accounts reflects the fact that in carrying out its programs and activities the Government sets up or creates various agencies, boards and commissions such as the Manitoba Crop Insurance Corporation, the Universities Grants Commission and the Workers' Compensation Board. The Government also sets up Crown corporations to carry out activities which are in the nature of business enterprises. The Manitoba Hydro-Electric Board and the Manitoba Telephone System are two examples of such business type enterprises. The Government often advances funds to these separate entities on which it earns an interest return. These advances, in turn, constitute part of its financial assets offsetting its liabilities.

In addition to the various budgetary and financial reports which the Government of Manitoba issues, there are two other sources of information on the Government's finances. The Public Finance Division of Statistics Canada issues a number of different reports which describe the

financial affairs of the provinces and the federal government on a comparable basis.¹ In addition, the National Accounts Division of Statistics Canada prepares a report on the finances of each of the provincial governments on a "national accounts" basis. Some reference will be made below to each of these reports as well.

The set of financial documents issued by the Manitoba Government and described above serve a number of different purposes. A primary purpose is to enable the Legislature to control the raising and expenditure of public funds. To facilitate this purpose, Members of the Legislature should receive information on various programs and activities in sufficient detail, consistent with reasonable cost, to enable them to assess the effectiveness and efficiency of government expenditures. This same information may also be desired by various members of the voting public and by analysts of government operations. Another purpose of these reports is to provide information useful for making economic decisions. The Government itself will require this information in formulating its economic policies. A wide range of users will be interested in analyzing and evaluating the impact of the Government's Budget upon the economy. Another important user of these data is the investment community including underwriters, credit rating agencies, potential bond buyers and present bondholders.

1. The reports which deal specifically with the provinces are as follows: Provincial Government Finance - Revenue and Expenditure (Estimates), Cat. No. 68-205; Provincial Government Finance - Revenue and Expenditure Cat. No. 68-207; Provincial Government Finance - Assets, Liabilities, Source and Application of Funds, Cat. No. 68-209 and Provincial Government Enterprise Finance, Cat. No. 61-204.

At the present time, the budgetary accounting approach followed by the Province is essentially the one described by the Canadian Institute of Chartered Accountants as the "net debt approach".² No distinction is made between current and capital expenditures. All expenditure on fixed capital assets are written off in the year in which the expenditure is made and no record is kept of these assets in the statement of assets and liabilities. However, a separate "Statement of Construction and Physical Assets" is maintained and presented in the Public Accounts. This statement provides an annual measure of gross capital formation. Since there are no complete and systematic estimates of depreciation of the Government's capital assets, there is no attempt to measure net additions to the Government's capital stock.

The Government of Manitoba does not keep a balance sheet in the normal sense, but presents "a statement of liabilities less recorded assets" in which the assets are limited to those which are entirely financial in character. For most governments, the net balance in this statement shows a net debt position. The net debt increases each year by the amount of the Government's deficit or declines by the amount of any surplus, where the deficit or surplus reflects the difference between all revenues and all expenditures, current and capital.

2. See Financial Reporting by Governments: A Research Study, The Canadian Institute of Chartered Accountants, 1980.

One of the major issues in government budgetary accounting is the way capital expenditures are to be handled. The present accounting treatment of capital expenditures was adopted in 1978-79. The new approach had been recommended by the Provincial Auditor and was viewed sympathetically by the Canadian Institute of Chartered Accountants in its publication Financial Reporting by Governments. It is a method now followed by many of the provincial governments in Canada, the principal exceptions being those in the Atlantic provinces. Prior to this change, separate funds had been maintained for current and capital expenditures. Funds approved for capital proposes did not lapse at the end of the fiscal year. This created an incentive to transfer unexpended funds in the current Budget over to the capital Budget where they could be carried forward to the following fiscal year. Under these arrangements, funds could be carried forward for many years. In contrast, with the present accounting treatment, all unexpended funds lapse at the end of the fiscal year and new authority is required from the Legislature after approval by the Treasury Board and Cabinet before further expenditures can be made.³

This change in the treatment of capital expenditures and a number of other recent changes in the Government accounts, such as the abolition of the longstanding Special Municipal Loan and General Emergency Funds and the discontinuance of the revolving account for the Queen's Printer were made

3. An exception to this is expenditures under special warrant approved by the Lieutenant-Governor and Council when the House is not sitting.

primarily to improve legislative control over the raising and expenditure of public funds. Two of the central concepts which are basic to this control are (1) a consolidated fund for all government revenues and expenditures and (2) annual approval of expenditures by the Legislature. Under a Consolidated Fund all government receipts go into a single consolidated fund. Expenditures out of this fund can only be made in accordance with annual estimates submitted to and approved by the Legislature with expenditure authority lapsing at the end of each fiscal year. In earlier years, this strict accountability to legislative control was weakened by a variety of devices. As was explained above, capital expenditures could be made under estimates approved in earlier years. Again, where revolving funds were in effect, revenues received by special agencies could be spent without legislative approval. Further details on some of the changes made during the past few years are given in Appendix A.

Without denying the importance of maintaining effective legislative control over public expenditures, it is necessary to recognize that the Public Accounts have other important uses. The form and presentation of accounts suited to the most effective legislative control may not be the most desirable for showing the economic impact of the Budget or in providing the information desired by economic or financial analysts. It may be that no single approach can adequately serve all these different uses. As will be suggested below, a compromise solution may be to supplement the present emphasis on legislative control with additional data that will better serve the needs of effective economic analysis. It should

also be recognized that effective legislative control of public expenditures is a complex issue. No simple set of rules can easily achieve the goal of economy and efficiency in government expenditures. Some of the largest expenditures such as those under the hospitalization and medical care plans take place under continuing programs where the size of annual expenditures cannot be easily scrutinized or controlled by the Legislature. Once the terms of payment for a program has been established, the size of actual expenditures will depend on a variety of economic circumstances not directly subject to the Government's control. Let us now consider the issue of the capital Budget in more detail.

The Capital Budget Approach to Government Accounting

When an individual has to make a major capital expenditure such as the purchase of a house for the first time, he will normally finance it by taking out a mortgage covering a large part of the purchase price. Very few individuals are in a position to pay for a house in cash or to finance it entirely out of current income. Frequently, the mortgage will be paid off in a series of monthly amortization payments over a period of 20 or 30 years.

Often a smaller governmental unit such as a village or town, when faced with a large capital expenditure such as a sewage treatment plant or a major street improvement program, will find itself in a position similar to that of an individual. To finance the project entirely out of current

revenues would impose an extreme if not impossible burden on its current residents. Moreover, given the fact that the capital facility will be in service for many years, it would be unfair as between present and future residents to impose the entire cost on people living in that locality at the time the project is undertaken. Thus, it is normal to finance these projects out of borrowed funds, with the resulting debt being amortized over a period of years.

For a larger governmental unit such as a major city or a province, capital expenditures often assume a more regular character. According to one estimate, during the 1970's the capital expenditures of the Government of Manitoba varied within the range of 1.03 and 2.14 percent of Gross Provincial Product. For these larger governmental units, the budgetary treatment followed is more optional. On the one hand, the Government can allocate these expenditures to a capital account and charge an amount equal to the depreciation on its capital assets to the regular Budget. Alternatively, it can treat all capital expenditures as if they were a current expenditure, charging them off in the year in which the expenditure is made. This is the treatment followed by the Government of Manitoba at the present time.

Even where no formal estimate of depreciation on capital assets is recorded, if capital expenditures are financed through borrowing, and the debt is amortized over a period of years, the amortization of principal may approximate to a charge for depreciation or capital consumption. However,

the extent to which these amortization payments cover actual depreciation is more or less accidental. The size of the amortization payments depends on the way capital expenditures happened to be financed and the length of the amortization period used.

In order to assess the implication of these two approaches, consider the data given in Table 1 which presents for Manitoba, by 5 year periods from 1961 to 1980, estimates of government capital formation, capital consumption allowances, net capital formation and the deficit or surplus that would be shown a) under the capital budgeting approach and b) under the present budgetary approach. The data are taken from Statistics Canada's Report on Provincial Economic Accounts.

TABLE 1. CAPITAL FORMATION, CAPITAL CONSUMPTION ALLOWANCES AND BUDGETARY SURPLUS OR DEFICIT, PROVINCE OF MANITOBA, 1961 TO 1980

<u>Years</u>	<u>Gross Capital Expenditures</u>	<u>Capital Consumption</u>	<u>Net Capital Expenditures</u>	<u>Budgetary Deficit or Surplus</u>	
				<u>a) Capital Budget</u>	<u>b) Current Practice</u>
Million Dollars at Current Prices					
1961-65	185	57	128	74	-54
1966-70	327	93	234	346	112
1971-75	420	177	243	144	-99
1976-80	595	325	270	436	166
1961-80	1,527	652	875	1,000	125
Million Dollars at Constant 1981 Prices					
1961-65	711	219	492	270	-222
1966-70	1,041	295	746	1,095	349
1971-75	994	398	596	472	-124
1976-80	797	437	360	540	180
1961-80	3,543	1,349	2,194	2,377	185

SOURCE: Statistics Canada, Provincial Economic Accounts, Cat. No. 13-213.

NOTE: All data are on a calendar year national economic accounts basis. For purposes of this table, amounts shown separately for hospitals were consolidated with those of the Provincial Government. Data were converted to 1981 prices using a Statistics Canada price series for Government capital expenditures.

As these data show, over the 20 year period 1961 to 1980, the Province of Manitoba carried out capital expenditures of about \$1.5 billion. In terms of 1981 prices, the capital projects involved would have cost over \$3.5 billion. After making allowance for depreciation there was a net addition to the stock of government owned capital assets of about

\$1 billion. Translated into equivalent 1981 prices, these data show that the Province made a net addition to its stock of capital amounting to about \$2.2 billion. With the budgetary approach currently in use, where no account is taken of capital consumption and capital expenditures are charged off as though a current expense, the Budget shows a net surplus of \$125 million over the 20 year period. In contrast, if the capital budget approach is used, the recorded surplus over the period amounts to about \$1 billion. When all the data are converted to 1981 prices, the accumulated surplus amounts to \$185 million under current budgetary practice and to just under \$2.4 billion with a capital budget approach. The difference between these two figures matches exactly the estimated net addition to the stock of government owned capital.

It should be noted that these data are estimated on a somewhat different approach than the regular budgetary accounts. Capital expenditures, for example, only includes newly produced physical capital assets. Acquisition of land or other existing assets are not included. Government revenues include contributions to pension funds of their employees as well as tax and other revenues. This approach, known among economists as the national accounts approach, is believed to provide a better measure of the economic impact of government expenditures and revenues than is shown by the regular accounts.

Examination of the data in Table 1 by 5 year periods reveals that capital expenditures were at their highest level in real terms during the

period 1966-1970. Co-incidentally, the budgetary surplus, also in real terms, reached its peak in that period as well. The capital expenditures in Table 1 cover physical capital assets only. Undoubtedly, government expenditures over the two decades from 1961 to 1980 also made a significant contribution to building up the stock of human capital in the Province, human capital in the form of the education, training and health of the people of Manitoba. However, since this type of capital is so difficult to measure, and because it may readily move out of the Province, no attempt has yet been made to measure and record this aspect of capital formation in the Province. Nevertheless, it should be emphasized that the skills and educational level of the Province's labour force are an extremely important asset that can play a vital role in the Province's future growth and development. It may prove desirable at some future date to provide estimates of this form of capital.

In the light of these data, what particular merit is there in the capital budget approach? A fundamental issue is the way in which the stock of government owned capital is recorded and accounted for. There can be no doubt that the social capital provided by the Government -- the roads, highways and bridges, the schools and hospitals, the parks and playgrounds, the flood control measures and drainage networks, the various office and other public buildings -- make an important contribution to the well-being and efficient functioning of the provincial economy. The present accounting approach all but neglects these assets. Even the budgetary approach which was in effect prior to 1978-79, which maintained a separate capital

division, did not provide for a systematic record of both gross and net capital formation and of the resultant changes in the stock of government owned assets.

From an economic viewpoint, leaving aside considerations of fiscal policy, the stock of government owned capital should be increased according to the same considerations which determine privately owned capital assets. Both publicly and privately owned capital should be increased up to the point where the net return to the marginal additional capital asset yields a social and private return just matching the real interest cost of the funds required to finance it. Because the return to government owned capital cannot be measured precisely, this criteria for public investment can only be applied on a rough and ready basis. In addition, considerations of fiscal policy would suggest that the Government's capital spending should be varied cyclically, being increased in periods of economic slack, and reduced in periods of economic expansion when private capital spending is more buoyant.

In applying the above approach to government economic policy making, it is not essential that the Government's accounting practice be converted back to a capital budgetary approach. The goals of effective economic policy making and accurate economic analysis can be adequately served if the Government maintains and presents, on an annual basis, government expenditures for new capital assets on a gross and net basis and shows the effects this will have on the Government's surplus and deficit in

a manner similar to that shown in Table 1. It would be desirable to have such data calculated both in terms of current and constant prices. For these purposes, estimates of depreciation should be prepared on a current replacement cost basis. To measure accurately the net addition that current capital expenditures make to the stock of government owned capital, it is necessary to have an estimate of the depreciation that has occurred on the existing stock of capital during the preceding year, also measured at current prices. This will require a revaluation each year to current prices of the existing capital stock and an estimate of how much that stock has depreciated. It is relevant to note that the Canadian Institute of Chartered Accountants has recently recommended that business enterprises with publicly traded securities should disclose as supplementary information the effects of inflation on the company's income statement and balance sheet. Implementation of these recommendations would result in the estimation of depreciation and the valuation of inventories, plant and equipment on a current replacement cost basis. (See filing instruction No. 41, C.I.C.A. handbook, December, 1982).

Assets and Liabilities

At the present time, the Government of Manitoba does not maintain any formal systematic record of its physical capital assets. The balance sheet entries presented in the Budget are limited to a record of its "liabilities less recorded assets." The recorded assets are mainly

financial consisting of cash, various accounts receivable, advances to crown corporations, agencies, boards and commissions and some longer term investments consisting of shares and debentures in crown corporations such as the Manitoba Forestry Resources Limited and the Manitoba Development Corporation. Its liabilities consist of its bonds, debentures and other securities less sinking funds -- this is often called the direct debt -- and some shorter term liabilities such as bank overdrafts and accounts payable. In addition, the Government reports separately guaranteed securities issued by its crown corporations. The guaranteed debt consists principally of securities issued by the Manitoba Hydro-Electric Board, the Manitoba Telephone System, the Manitoba School Financing Authority and the Universities. Fixed capital assets have been written off and are carried at nominal values only.

Prior to the accounting changes made in 1978-79, for many years the Government did present a balance sheet which recorded fixed capital assets as well as financial assets. However, the information provided on government owned fixed capital assets was not very meaningful. For the most part, assets were only recorded where outstanding debt had been designated as having been used to finance certain assets. The figure shown for any asset represented an historic cost only. No attempt was made to show the current replacement cost of the asset. The balance sheet did not begin to present a complete record of the Government's capital assets.

As of March 31, 1982, the excess of liabilities over recorded assets reported by the Province of Manitoba amounted to \$1,091 million.

This is clearly the best measure of the Province's direct debt position. In addition, there were guaranteed and indirect liabilities (net of sinking fund assets) amounting to \$1,822 million. The total direct and indirect debt (net of sinking funds and various advances and other financial assets) amounted to some \$2,913 million. Offsetting this, in a complete balance sheet presentation, would be all the real capital assets owned directly by the Government and its equity ownership in various crown corporations. It was noted above that one estimate of the net addition to government owned capital assets (at 1981 prices) over the period from 1961 to 1980 amounted to some \$2.2 billion. In addition, if the real assets owned by the Government's two major crown corporations, Manitoba Hydro and the Manitoba Telephone System, which had a book value of \$3,135 billion on March 31, 1982, were valued at their current replacement cost, this would add from \$2 to \$3 billion to the above total. Thus, a realistic balance sheet for the Province would show a substantial excess of assets over liabilities. Table 2 provides such a balance sheet on a tentative basis. As these data show the total value of the Government of Manitoba's assets, when valued at current prices, exceeds its direct debt by an amount in excess of \$6 billion. And this total does not assign any value to the huge amount of crown land owned by the Province. Further work will make it possible to produce a more precise estimate of the Province's asset position.

TABLE 2

GOVERNMENT OF MANITOBA

Tentative Balance Sheet as of March 31, 1982
(Million Dollars)

Assets

Financial Assets ¹	\$2,379.9
Physical Assets	
Highways and Bridges ²	3,000.0
Buildings and Contents ³	544.8
Universities, buildings, land and equipment ⁴	236.2
Hospitals ⁵	150.3
Schools ⁶	490.7
Crown lands ⁷	No value assigned
Net equity in Manitoba Hydro ⁸	2,700.0
Net equity in Manitoba Telephone System ⁸	199.2
Water Rights ⁹	No value assigned
Total Assets	<u>\$9,701.1</u>

Liabilities

Bonds, debentures and other direct debt	\$3,471.0
Excess of Assets over Liabilities	<u>\$6,230.1</u>

NOTES:

1. As reported in Public Accounts, 1981-82, p. 1-5
2. Values are estimated replacement values at today's costs.
3. Asset values are at estimated replacement cost based on data compiled for insurance purposes. Buildings whose value is estimated to be less than \$500,000 are not included. The total includes the community colleges and special schools operated by the Province.
4. Data are reported book values as of March 31, 1981.
5. Winnipeg hospitals only, valued at historical cost.
6. Original cost after depreciation as at December 31, 1981.
7. While no value has been assigned to crown land, some 40 million out of the 55 million hectares of land in Manitoba belong to the Government. Provincial parks utilize 1.1 million hectares, wildlife management areas, 1.1 million, provincial forests .9 million, and .8 million hectares are used for hay production, livestock grazing and annual cropping.
8. Value of assets at current replacement cost less values recorded on company's balance sheet plus reserves.
9. At the present time only about one-third of Manitoba's potential hydro-electric power has been developed. In addition, Manitoba has vast areas of freshwater in lakes and streams.

In addition to the data presented in Table 2, it may be desirable to present an annual balance sheet covering the public sector for the Province as a whole. This would consolidate into one balance sheet public assets and liabilities in the Province including the City of Winnipeg. Again, it would be desirable to have assets reported in this balance sheet at an estimated current replacement cost. The inflation of recent years has greatly increased the difference that exists between the original cost of assets and their value at today's prices. The public sector would include the universities, the school divisions and the hospitals.

The Public Accounts and the Budget Speech should present information which will allow the interested reader to evaluate the debt position of the Government. In making this evaluation, it is important to consider the Government's accumulated debt in the light of both a) the past and prospective growth of the economy and b) the effects that inflation has had in distorting the Government's fiscal position. As will be noted below, inflation distorts the Government's reported deficit or surplus as well. Let us consider each of these considerations in turn.

The Effects of Real Income Growth on the Province's Financial Position

When the real income level in a province is growing, it is possible for its government to run a continuous annual deficit (on average) without any increase in the ratio of debt to provincial income. In order to separate out the effects of real income growth from inflation, let us assume

an absence of inflation. Now suppose the government deficit as a percent of provincial income remains constant and is represented by $\underline{d}$. Then, if real income is growing at a constant rate $\underline{r}$, it can be shown that the ratio of debt (D) to income (Y) will eventually approach the ratio $\underline{d}/\underline{r}$.⁴ Suppose, for example, $\underline{d}$ were 2.0 percent of provincial income and income was growing at 4.0 percent a year, the ratio D/Y, debt to income, will approach $2/4$ or .5. That is, accumulated debt will eventually amount to about 50 percent of provincial income. This means that provided real income continues to grow at this same rate the government could run a deficit, equal to 2 percent of its income, more or less indefinitely without causing any increase in the debt burden as measured by the ratio of debt to income. In addition, if the rate of interest on the government's bonds remained constant at $\underline{i}$, the ratio of interest payments (I), that is, net debt charges, to income (Y) would approach and remain at the constant ratio, $I/Y = \underline{d} \cdot \underline{i}/\underline{r}$. If the yield on the government's bonds in the above example were 3.5 percent, the ratio of interest payments to income would be 1.75 percent (0.5×3.5).

Applying this model to the Province of Manitoba, we find that Real Provincial Product has grown at an annual rate of 3.7 percent over the period from 1961 to 1980. In addition, we know that over the decade ending in 1962, the yield on Government of Manitoba bonds averaged about 4.5 percent. Since the average annual inflation rate over the decade ending in

4. See C.L. Barber, The Theory of Fiscal Policy as Applied to a Province, Ontario Committee on Taxation, 1966, Chapter 5.

1962 was about 1.0 percent, the real interest rate would have amounted to about 3.5 percent (where the real interest rate is defined as the nominal rate less the rate of inflation). Over the 24 year period from 1958/59 to 1981/82, the average deficit of total expenditures over total revenues for the Province amounted to about .57 percent of provincial income. On this basis, the expected ratio of debt to income (D/Y) would be .154, that is, the province's direct debt would amount to about 15.4 percent of provincial Gross Provincial Product. In fact, the ratio was only 7.9 percent. This difference undoubtedly reflects the effects of inflation, to a consideration of which we now turn.

The Effects of Inflation on Various Measures of the Province's Financial Position

It is well known that inflation benefits debtors and hurts creditors, for it allows the debtor to pay off his debt with dollars whose real value has declined. However, this effect may be partially or even fully offset by the level of interest rates. When inflation is fully anticipated, economists argue that nominal interest rates include an inflation premium which compensates the lender for the decline in the real purchasing power of his loan as a result of inflation. Thus, if the non-inflationary or real rate of interest was 4 percent and the inflation rate expected over the life of the loan was 10 percent, a nominal rate of 14 percent (assuming the interest income was not taxable) would compensate the lender fully for the decline in the real value of his asset and yield him a

real rate of return of 4 percent. No one can be sure how much of any interest rate reflects an inflation premium and how much a real rate of interest, but there can be little doubt that in the past few years as high as two-thirds of interest payments have been an inflation premium, a compensation to the bondholder and other debtors for the decline in the real value of their assets. This part of current interest payments can be considered a kind of advance repayment of the debt (in real terms) rather than a current expenditure. The inclusion of the entire interest expense in the Government's Budget exaggerates the size of the deficit.

Most economists now agree that government Budgets should be adjusted for these distorting effects of inflation. Because interest expenditures are now such a large component in government Budgets -- for all governments in Canada, on a gross basis, interest payments currently exceed \$25 billion -- the result is to greatly exaggerate the size of government deficits. The Department of Finance in Ottawa recently estimated that on an inflation adjusted basis the federal deficit for 1982 would be some \$7 billion less than the amount currently reported.

Let us consider the implications of such an inflation adjustment for the Province of Manitoba covering the fiscal year ended March 31, 1981. The amount of the inflation adjustment can be estimated in two different ways. These are as follows:

- a) The first approach involves a consideration of the interest payments made by the Province. The following are some relevant data:

Fiscal Year Ended March 31, 1981
(Thousand Dollars)

Gross Interest and Debt Charges	524,111
Interest Receipts	149,169
Net Interest Payments	374,942

(A more complete statement of these data is given in Appendix B.)

As these data show, during the fiscal year ended in March, 1981, the cost to the Province of servicing its direct and guaranteed debt amounted to \$524 million. This includes the debt of Manitoba Hydro, the Manitoba Telephone System and all other government agencies. Offsetting this, the Province earned \$149 million on various investments, advances to its own agencies or other financial assets. Thus, its net cost of servicing various debts amounted to about \$375 million. If the expected inflation rate is taken as equal to the average rate in Canada over the 5 year period from 1976 to 1980, it would be equal to 8.8 percent. The yield on long-term provincial government bonds for the 12 months ended in March, 1981, was about 13.2 percent. Thus, the 8.8 percent expected inflation rate is about two-thirds of this 13.2 percent yield. This suggests that about \$250 million of the \$375 million net debt servicing cost can be considered an inflation premium needed to compensate the bondholder for the decline in the real value of his asset.

b) A second approach to this problem is to consider how much the Province gained as a creditor during the fiscal year. For the 12 months ending in March, 1981, Canada's inflation rate was 12.5 percent. If we apply this to the Province's outstanding debt at the fiscal year-end, some \$2,680 million, we obtain an estimated gain of \$355 million.⁵ However, this approach would be valid only if the entire debt were payable in Canadian dollars. If we apply to the debt held in foreign currency the inflation rate of that country, the net gain to the Province amounts to just \$270 million. This estimate assumes that the net direct debt and the guaranteed debt of the Province can be considered as in effect almost all foreign denominated, bonds issued in Canadian dollars being roughly offset by financial assets denominated in Canadian dollars.

If we average the above two estimates, we obtain an inflation adjustment of \$260 million. Because this estimate includes the debt issued by the Province's major crown corporations as well as other agencies, the adjustment does not apply fully to the regular budgetary deficit. It is, nevertheless, a benefit to the Province which should be recognized in assessing its net debt position.

4. The outstanding debt is taken as the excess of liabilities over recorded assets, \$822 million, plus guaranteed and indirect liabilities net of sinking funds, \$1,858 million.

**TABLE 3 NET DIRECT DEBT IN RELATION TO GROSS PROVINCIAL PRODUCT,
MANITOBA, 1959 TO 1982**

	<u>Net Direct Debt</u> (\$ million)	<u>Percent of G.P.P.</u>		<u>Net Direct Debt</u> (\$ million)	<u>Percent of G.P.P.</u>
1959	190.1	10.4	1971	204.5	5.1
1960	216.1	11.2	1972	220.9	5.0
1961	245.1	12.9	1973	203.0	3.8
1962	263.3	12.5	1974	207.3	3.3
1963	272.6	12.5	1975	260.0	3.7
1964	289.0	12.1	1976	353.6	4.4
1965	291.1	11.4	1977	430.2	5.0
1966	300.9	11.0	1978	621.5	4.6
1967	302.9	10.1	1979	705.8	6.8
1968	281.1	8.5	1980	750.6	6.7
1969	260.1	7.4	1981	840.1	6.4
1970	234.6	6.4	1982	1,091.1	7.9 prelim.

NOTE: Direct debt was estimated by adjusting the excess of liabilities over recorded assets as reported at March 31, 1982 by the deficit or surplus in the preceding fiscal years.

Both the real income effect and the inflation adjustment effect show up in implicit form when we compare the Province's debt with provincial income. Thus, as the data in Table 3 show, over the 24 year period, 1959 to 1982, the Province of Manitoba's net direct debt (the excess of liabilities over recorded assets) reached a peak in relation to Gross Provincial Product of 12.9 percent in 1961, thereafter it declined steadily, reaching a low point of 3.3 percent in 1974. Since then, there has been a moderate increase in this ratio to an estimated 7.9 percent for 1982. In absolute dollar terms, the net debt increased some \$884 million over the past 8

years, yet because of the relatively high rate of inflation that was occurring, the debt to income ratio rose only moderately. However, it must be emphasized that once interest rates move up to levels that fully anticipate the higher rate of inflation, inflation may no longer have any net effect on the debt to income ratio. This will be true if the higher interest payments result in correspondingly higher Budget deficits.

The deficits and surpluses recorded by the Province of Manitoba, estimated on the basis of current budgetary procedures are set forth in Table 4 along with estimates of the Gross Provincial Product and, for part of the period, for total provincial revenues and expenditures. It was this set of estimates of provincial deficit or surplus that were used in estimating the Province's net direct debt position shown in Table 3.

TABLE 4 MANITOBA'S COMBINED DEFICIT AS A % OF GPP, REVENUES AND EXPENDITURES

Fiscal Year	Calendar Year	A (Deficit) Surplus \$M	B GPP \$M	C Revs \$M	D Expend \$M	A/B %	A/C %	A/D %
1958/59	1958	(7.4)	1,682			(0.4)		
1959/60	1959	(26.0)	1,835			(1.4)		
1960/61	1960	(29.0)	1,928			(1.5)		
1961/62	1961	(18.2)	1,893			(1.0)		
1962/63	1962	(9.3)	2,109			(0.4)		
1963/64	1963	(16.4)	2,174			(0.8)		
1964/65	1964	(2.1)	2,394			(0.1)		
1965/66	1965	(9.8)	2,550			(0.4)		
1966/67	1966	(2.0)	2,735			(0.1)		
1967/68	1967	21.8	2,994	370.8	349.0	0.7	5.9	6.2
1968/69	1968	21.0	3,289	421.8	400.8	0.6	5.0	5.2
1969/70	1969	25.5	3,492	511.7	486.2	0.7	5.0	5.2
1970/71	1970	30.1	3,674	604.6	574.5	0.8	5.0	5.2
1971/72	1971	(16.4)	4,069	640.9	657.3	(0.4)	(2.6)	(2.5)
1972/73	1972	17.9	4,477	746.5	728.6	0.4	2.4	2.5
1973/74	1973	(4.3)	5,360	866.4	870.7	(0.1)	(5.0)	(0.5)
1974/75	1974	(52.7)	6,293	1,011.4	1,064.1	(0.8)	(5.2)	(5.0)
1975/76	1975	(93.6)	7,120	1,206.1	1,299.7	(1.3)	(7.8)	(7.2)
1976/77	1976	(76.6)	7,960	1,395.5	1,472.1	(1.0)	(5.5)	(5.2)
1977/78	1977	(191.3)	8,610	1,444.3	1,635.6	(2.2)	(13.2)	(11.7)
1978/79	1978	(84.3)	9,420	1,550.8	1,635.1	(0.9)	(5.4)	(5.2)
1979/80	1979	(44.8)	10,340	1,806.0	1,850.8	(0.4)	(2.5)	(2.4)
1980/81	1980	(89.5)	11,190	1,968.4	2,057.9	(0.8)	(4.5)	(4.3)
1981/82	1981	(251.0)	13,100	2,180.8	2,431.9	(1.9)	(11.5)	(10.3)

SOURCE: Department of Finance.

NOTE: Revenue, expenditure and deficit surplus figures shown have been recast back to 1967/68 on a basis consistent with present accounting practices. Comparable data on revenue and expenditure for the period prior to 1967/68 are not currently available. However, the deficit/surplus figures for years prior to 1967/68 are comparable with those for subsequent years. Gross Provincial Product estimates shown are from various Manitoba Budget Addresses.

Issues Related to Foreign Currency Borrowing

In view of the fact that on a net basis the Province of Manitoba's direct and guaranteed debt can be considered as being almost entirely denominated in foreign currencies, it is desirable to consider some of the issues involved in such borrowing. In recent years the yield differentials on long-term government bonds have been quite substantial. The following are the yields that prevailed in July, 1982 for four countries from which Manitoba has borrowed substantial amounts in the past.

YIELDS ON GOVERNMENT BONDS, JULY, 1982

	<u>Yields</u>	<u>Differentials</u>
Canada	15.62	
Japan	8.34	-7.28
West Germany	9.30	-6.32
Switzerland	4.90	-10.72
United States	13.76	-1.86

As these data show, the yield differentials in July, 1982 varied from a low of 1.86 percentage points as between Canada and the United States and a high of 10.72 between Canada and Switzerland.

If exchange rates could be expected to remain fixed these interest differentials would provide very substantial interest savings over the life of a long term bond issue. However, today's world is one of fluctuating exchange rates. Moreover, interest rate differentials exist in very considerable degree because of different expected inflation rates in the various countries. If one country consistently has a higher inflation rate

than another, one may expect the exchange values of the two currencies to reflect that difference. This relation will not be exact because exchange rates reflect a variety of other economic factors in addition to underlying inflation rates. Still, as inflation rates have increased, the inflation rate differential has become an increasingly important factor in influencing exchange rate levels.

Some data illustrating this relationship is given in Table 5. The data compare Canada with the four countries of United States, West Germany, Japan and Switzerland.

TABLE 5 INFLATION RATE DIFFERENTIALS AND CHANGES IN EXCHANGE RATES, CANADA COMPARED WITH FOUR OTHER COUNTRIES, 1957 TO 1982

Inflation Differentials: Canada Minus Foreign Rate

	<u>1957-1982</u>	<u>1972-1982</u>	<u>1977-1982</u>
United States	+0.1	+0.5	+0.4
West Germany	+1.5	+3.8	+5.5
Japan	-1.3	0.0	+5.9
Switzerland	+1.3	+4.0	+6.1

Annual Increase in Canadian Dollar Price of Foreign Currency

	<u>1957-1982</u>	<u>1972-1982</u>	<u>1977-1982</u>
U.S. Dollar	1.01%	2.24%	3.05%
German Mark	3.09	4.63	1.30
Japanese Yen	2.20	3.44	2.98
Swiss Francs	3.93	8.51	6.15

NOTE: Inflation rate differentials are based on the Consumer Price Index. Annual increase in foreign currency prices are compound annual increase in percentage terms.

SOURCE: Data taken from International Financial Statistics, International Monetary Fund.

An examination of Table 5 shows that the increased cost of foreign currency in Canadian funds can very significantly affect the cost of foreign borrowing. For example, the lower interest cost of a loan in Swiss francs in 1972 would have been offset over the past ten years by an average annual increase of 8.5 percent in the Canadian dollar price of Swiss francs. In principle, the Province will find there is an advantage in borrowing in a foreign currency if the real interest cost, that is, the nominal interest rate less the expected rate of inflation, is significantly lower. Over a

long period of years, Canadian and United States inflation rates have been very similar. To the extent that this pattern can be expected to continue, differences in nominal interest rates in the two markets can be taken as a reasonable measure of differences in real rates. But in recent years, inflationary forces have increased and this has introduced an increased degree of uncertainty as to the advantages involved in any foreign loans. The risks involved in these transactions are undertaken by the borrower.

How should the costs involved in a change in foreign exchange rates be treated from a budgetary viewpoint? When Canadian funds are borrowed at a higher interest cost reflecting the higher rate of inflation in Canada, all of this interest expense appears in budgetary expenditures or in the interest costs to government owned crown corporations. If the Government borrows abroad with an annual saving of 6 or 7 percent or more, as would be true today if the bonds were issued in German, Japanese or Swiss currencies, only the lower interest costs will appear in the Budget plus additional foreign exchange costs on this annual interest payment. The additional cost that the foreign exchange rate has on the Canadian dollar valuation of the outstanding foreign currency debt may be deferred until the date at which the original bond issue is redeemed. This might involve large additional costs in particular years. An alternative approach would be to amortize these additional costs as they occur over the remaining life of the loan. This would bring annual debt charges more closely in line with the costs that would be incurred if all borrowing took place in Canadian funds. It should be recognized that this additional foreign exchange cost

corresponds more or less closely to the inflation premium in interest rates referred to above. More precisely, it corresponds to that part of the premium which reflects the difference in inflation rates. It was argued above that the inflation premium in interest rates is essentially a capital transaction rather than a current expense. Accordingly, it would be appropriate to regard this foreign exchange loss or gain on outstanding bonds as a capital transaction also.

The Current Deficit

When the Government of Manitoba presented its Quarterly Financial Report covering the first six months of the current fiscal year, it projected a deficit for the entire year of \$498 million. This was an increase of some \$155 million as compared with the estimates presented in the Budget Speech. How was this increase in the deficit to be viewed? Did it reflect a major increase in government expenditures? Or significant tax cuts? Or was it simply a reflection of the way government expenditures and revenues changed in the face of the most serious recession since the 1930's?

Economists find it useful to calculate a high employment budgetary deficit. This shows the expenditure and revenue totals that could have been expected to prevail if the economy had continued to operate at a certain level of output and employment. This concept enables economists and others to distinguish between what some have called an "active deficit" and a "passive deficit". If the increase in the Government deficit is entirely

the result of a decline in economic activity which causes revenues to fall and welfare and similar payments to increase, the resulting change is labelled a "passive increase in the deficit". It is an increase which occurs without any government program or policy changes. On the other hand, if the increase in the deficit results from a planned increase in government spending or a deliberate tax cut, the change is considered to be an "active increase in the deficit". Deliberate changes of this type will change the high employment deficit or surplus. A passive increase in the deficit will have no effect on the high employment budgetary position.

The level of output and employment chosen as a high employment position is to some degree arbitrary. The Department of Finance in Ottawa publishes what they term a "cyclically adjusted deficit". For their latest estimate, this series is based on an assumed 6.3 percent unemployment rate and a rate of productivity growth of 0.5 percent. In applying this concept, the Province of Manitoba might find it useful to use the average unemployment rate in Manitoba over the period 1977 through 1981 as a benchmark. It will be recommended below that a "high employment" or "cyclically adjusted" deficit or surplus be estimated on a regular basis both for the fiscal year just completed and for the forthcoming fiscal year. This will enable users of budgetary data to distinguish more easily between "active" and "passive" changes in the Government's budgetary position.

Recommendations

1. The Government should estimate and present its budgetary deficit or surplus on two different bases. Basis One would simply be a continuation of the approach adopted in 1978/79. Called the "net debt approach" by accountants, this approach compares all revenues and all expenditures without distinguishing between current and capital expenditures. Basis Two would be a form of the capital Budget. In this approach, expenditures would be separated into those which add to the stock of tangible physical assets, that is, capital expenditure so defined, and all other or current expenditures. This total should include capital assets created with labour and equipment employed directly by the Province as well as purchased assets and the value of contract construction. In applying this approach, estimates of depreciation on the Government's existing stock of capital should be prepared. These estimates should be on a current replacement cost basis. An amount of capital expenditures equivalent to this estimate of depreciation should be designated as a current expenditure. This represents the amount of capital expenditure needed to offset the depreciation in the Government's existing capital stock during the current fiscal year. The balance of total capital expenditures, the amount which represents a net addition to the Government stock of capital assets would be designated as net capital expenditure. The Budget would show the Government's surplus or deficit before these net capital expenditures. In applying this approach, careful consideration would need to be given to the range of different government agencies that would be covered by this estimate of capital

expenditures. Would it, for example, include capital expenditures by the universities, the hospitals and similar institutions?

2. The Government should present on an annual basis a balance sheet showing the Government's asset position. For purpose of this balance sheet, real assets should be included on a depreciated current replacement cost basis. The balance sheet should also include the Government's equity position in its crown corporations such as the Manitoba Hydro-Electric Board and the Manitoba Telephone System. This equity position should also be calculated with physical assets valued at a depreciated current replacement cost.

3. The Government should prepare and estimate on a regular basis a "cyclically adjusted or high employment budgetary statement of revenues and expenditures". This will enable users of Government budgetary data to distinguish more readily between active and passive changes in the deficit or surplus.

4. The Government should present each year as supplementary information an estimate of the effects of inflation on the financial position of the Province. Such an "inflation adjustment" was estimated in the body of this report for the fiscal year 1980/81. While this estimate cannot be made on any exact basis, in a period when the inflation rate is relatively high, the benefit to the Province's financial position has clearly been large.

5. No change is recommended in the Province's treatment of the effect of foreign exchange fluctuations on its "net debt charges". But as the analysis above emphasizes, the rise and increased variability of inflation rates through the world has increased the difficulty involved in accurately assessing the advantages to be gained from borrowing in one or more foreign currencies.

6. No changes are recommended in the general accounting approaches followed by the Government. The recommendations made above can be considered more statistical than accounting in nature.

7. In presenting its annual budgetary information, it would be helpful if data were also presented for a period of earlier years showing the level of revenues and expenditures relative to the level of Gross Provincial Product.

8. Information should also be provided on the ratio of the Province's debt position relative to the level of Gross Provincial Product, similar to the data given in Table 3.

APPENDIX A

SUMMARY OF CHANGES IN ACCOUNTING POLICY DURING THE
THIRTY-YEAR PERIOD 1953-54 TO 1982-83

Policy Change

Year of Change

A. Capital Division

- | | |
|--|---------|
| a) The Capital Division and Revenue Division of the Consolidated Fund were combined in order that the annual estimates of the Government would show all expenditure on Government programs and all revenue received by the Government. | 1978-79 |
| b) Buildings, highways and other fixed assets purchased out of Capital Division and previously carried at a value equal to the amount of outstanding debt assigned to them were written off. In future, all fixed assets will be written off when purchased. | 1978-79 |
| c) Amounts paid from Capital Division for Miscellaneous and Intangible Assets were previously recorded at a value equal to the amount of outstanding debt assigned to them. These amounts were reduced to | 1978-79 |

their expected recoverable value and in future will be recorded as an asset only to the extent that they represent a claim by the Government on other parties.

B. Surplus and Reserve Accounts

a) Prior to 1959-60, it was fairly common to transfer large amounts from the revenue division surplus account to the capital division for purposes such as:

Prior to 1959-60

a) the cost of specific capital expenditures

b) repayment of debt

In 1959-60, a different approach was taken whereby the excess of revenue over expenditure for one fiscal year was transferred to the subsequent fiscal year, and became part of the revenue of that fiscal year.

1959-60 and on

b) The various surplus accounts operated by the Government have been consolidated and now constitute a part of "The Excess of Liabilities Over Recorded Assets".

1978-79

c) Sinking Fund payments were previously shown as a 1978-79
statutory expenditure of the Government into a
Sinking Fund Reserve. The Reserve has been
eliminated and the annual expenditure is no longer
recorded. However, the practice of allocating money
into a separate fund so that it is designated for
the purpose of debt repayment has been continued.

d) Reserve accounts pertaining to gravel pits and road 1982-83
machinery were discontinued in order to improve
legislative control over the purchases of gravel
pits and road machinery by including these amounts
in the annual estimates of the Province.

C. Special Municipal Loan and General Emergency Fund

a) Expenditures which were previously made directly 1979-80
from the Special Municipal Loan and General
Emergency Fund are now budgeted and paid from a
departmental appropriation. The change was made to
allow more direct control over this expenditure by
the Legislature. Similarly, interest earned by the
fund on investments, loans and advances is now
recorded in the same manner as investment income.
The payments were made from appropriation 4(2) in

the Department of Labour and Manpower. The interest was recorded as a reduction of Public Debt Expenditure.

- b) The Special Municipal Loan and General Emergency Fund, which in previous years was treated as a reserve account and deducted from the "Excess of Liabilities Over Recorded Assets" account, has been abolished. This was accomplished by a transfer of the fund balance to revenue in accordance with the provisions of the Special Municipal Loan and General Emergency Fund Act. The result was an increase of revenue of \$24,966,733 for the 1981-82 fiscal year and an increase in the balance of the "Excess of Liabilities Over Recorded Assets" account for a corresponding amount.
- 1981-82

D. Advances to Crown Agencies

- a) In previous years debentures payable in the United States funds sold for The Manitoba Hydro-Electric Board purposes were recorded at par value with a corresponding amount charged as an advance to the Utility. Premiums arising from the conversion of United States dollars to Canadian dollars were paid
- 1969-70

to the Utility but were not recorded as an advance. During 1969-70, in accordance with requirements of The Financial Administration Act, premiums of \$10,040,430.77 were reflected in the accounts of the Province as an advance to the Utility with a corresponding amount credited to an account as a provision for premium on United States funds. However, the established policy continues to be that the Utility is responsible to provide sufficient funds in United States dollars to retire the debentures at maturity.

- b) An Allowance For Losses On Realization of Assets has 1978-79
been established to provide for the decreases in the
estimated realizable value of loans, advances and
investments because of accumulated deficits of the
Crown Corporations, Agencies, Boards and Commissions
in which the Government has invested money. This
allowance is adjusted annually for changes that may
occur in the estimated realizable value of these
assets.

E. Public Debt

- a) Debt discounts and premiums that resulted from the issue of provincial securities for a consideration that differs from the par value of the securities were previously amortized over the life of the respective securities. Underwriting commissions and similar expenses were treated as an operating expense of the year in which they are incurred. 1978-79
- b) Debentures payable in U.S. dollars were previously stated at the rate of \$1 U.S. equals \$1 Canadian whereas debentures payable in other foreign currencies were stated at the Canadian dollar equivalent based on the actual conversion of proceeds or at the exchange rate in effect at the date of issue if conversion did not take place at issue date. Debentures payable in U.S. dollars have now been adjusted to reflect the Canadian dollar equivalent value at time of issue and will in future be treated in a consistent manner with all other foreign issues. 1978-79

F. Queen's Printer

- a) The financial results of the Queen's Printer 1978-79
operations, which were previously calculated on an
accrual basis, have been converted to a cash basis
to make them consistent with the Government
Accounts.

- b) The practice of recording the receipts and payments 1978-79
of the Queen's Printer, Stores Stock Operation,
through a revolving account was discontinued in
1980-81. Previously, these transactions were
recorded in an Open Ledger Account and the net
result for the fiscal year was shown directly in the
"Excess of Liabilities Over Recorded Assets"
Account. In 1980-81, these transactions were
budgeted and recorded through appropriation 4(f) in
order that this operation would be included in the
total expenditure of the Province.

- c) The reserve account pertaining to Queen's Printer 1980-81
equipment was discontinued in order to improve
legislative control over the purchase of this
equipment by including these amounts in the annual
estimates of the Province.

G. Revenue and Expenditure Accounts

1. Gross Accounting Concept

- a) The Statement of Revenue and Expenditure for the 1966-67
fiscal year ended March 31, 1967, was prepared on a
"gross accounting" basis. The "gross accounting"
concept is designed to show gross expenditures made
with respect to each service; receipts including
those from participating authorities, are taken into
the revenues of the province. With the
implementation of this new concept, both the
revenues and expenditures for the year ended
March 31, 1967, reflect a substantial increase as
compared with those of the previous fiscal year.
- b) There was a change in the method of stating revenue 1976-77
from a gross cash basis to applying payments to
municipalities of \$17.5 million as a reduction of
revenue - Individual Income Tax by \$11.9 million and
Corporation Income Tax by \$5.6 million. This was
done in accordance with legislative amendment which
provided for direct payments to the Municipalities
equivalent to two points of Individual Income Tax
and one point of Corporation Income Tax. In prior

years these Unconditional Grants were shown as an expenditure out of a Municipal Affairs appropriation.

- c) The Individual Income Tax revenue was reduced in 1977-78 this fiscal year by \$127 million, being the amount of property tax credits and costs of living tax credits. In the preceding fiscal years these credits amounting to \$105.7 million were charged to an appropriation in the Department of Finance.
- d) Payments of \$63.6 million to the Manitoba Health 1977-78 Services Commission under the new Federal-Provincial Fiscal Arrangements and Established Programs Financing Act were applied as a reduction of the Individual Income Tax revenue in this fiscal year.
- e) The following items which were previously shown as a 1978-79 net reduction of revenue are now shown as expenditures in accordance with the Gross Accounting Concept:
- i) Tax Credit Payments - previously shown as a reduction of Individual Income Tax

- 11) Manitoba Health Services Commission - previously shown as a reduction of Individual Income Tax.

2. Cash or Accrual Accounting

- a) A significant change was made in 1968-69 in revenue accounting with the revenue being stated on a strictly cash basis in accordance with section 53 of the Treasury Act. As a result of this change, the practice of recording as revenue at the fiscal year-end the amounts then due from Canada in respect of shared-cost programmes has been discontinued. These amounts, totalling \$7,482,700.94 as at March 31, 1969, will now be recorded as revenue in the year in which actually received. 1968-69
- b) A significant change in accruals during the 1968-69 fiscal year resulted from the inauguration of the system of bi-weekly pay of salaries and wages. This new system replaced a system of semi-monthly pay with the result that employees were paid on the last or second last Friday in March, depending on the nature of employment. Salaries and wages in the amount of \$1,653,212.88 were accordingly accrued from the date of the last payment in March to March 31. 1968-69

- c) A decision was made to discontinue the practice of recording the inventory of supplies on hand as at the end of a fiscal year effective as at March 31, 1972. The inventory of supplies on hand, recorded as at March 31, 1971, amounted to \$1,190,290.48. 1971-72
- d) Accruals on municipal aid under The Social Allowances Act, assistance to nursing homes and school tax rebates were discontinued as at March 31, 1974. The reversal of accruals as at March 31, 1973 resulted in a decrease of \$2,059,396 in expenditures for the fiscal year ended March 31, 1974. 1973-74
- e) Revenue from shared-cost agreements with the Government of Canada, which was previously recorded only when the cash was received, will be recorded on an accrual basis commencing with the 1980-81 fiscal year. In order to make the transition from the cash to accrual basis, an adjustment was made at March 31, 1980 whereby the amount receivable from this source at that date was recorded through the "Excess of Liabilities Over Recorded Assets" Account. Footnotes explaining this change are found on the statement showing "Excess of Liabilities Over Recorded Assets" and on the schedule of operating 1979-80

fund assets and liabilities entitled "Advances and Other Receivables".

3. Miscellaneous

- a) In previous years an appropriation was provided for 1979-80 the refund of prior years' revenue whereas the refund of revenue received in the current year was treated as a reduction of the related revenue account. A change was made in 1979-80 to treat all revenue refunds on a consistent basis. In 1979-80, all revenue refunds, regardless of the year the revenue was received, are shown as a net reduction of the related revenue account. A footnote explaining this change is found on the "Statement of Revenue".
- b) The former Debt Retirement Reserve was transferred 1979-80 to and became a part of the Provincial Sinking Fund as at April 1, 1978. However, in 1978-79, the interest earnings of this reserve were still budgeted and recorded as a revenue of the Department of Finance. In 1979-80, these earnings are recorded as a reduction of the Public Debt expenditure so as to be consistent with other Sinking Fund earnings.

- c) The practice of recording the receipts and payments of the Veterinary Drug Centre and the Semen Distribution Centre through a revolving account was discontinued in 1979-80. The transactions of these two centres were budgeted and recorded through appropriations and revenue accounts in the Department of Agriculture in 1979-80 to allow more direct control by the Legislature over these operations. The payments were made from appropriations 8(g) and 8(h) in the Department of Agriculture; the revenue was deposited to Department of Agriculture, Miscellaneous Receipts for Sundry Services.

APPENDIX B

**CONSOLIDATION OF DEBT SERVICING COSTS
PAID BY THE GOVERNMENT AND ITS AGENCIES
DURING THE FISCAL YEAR ENDED MARCH 31, 1981**

		DEBT COSTS	INTEREST EARNINGS	NET COST
		(Thousands of Dollars)		
Public Debt Cost as per Public Accounts:				
Payments	258,173			
Recoveries from Agencies	<u>122,549</u>	135,624		
Investment Income			56,752	78,872
Hydro Rates Stabilization		10,804		10,804
Self-Supporting Debt:				
Manitoba Hydro		236,111	17,895	218,216
Manitoba Telephone System		51,775	7,738	44,037
Manitoba Water Services Board		2,568	1,396	1,172
Manitoba Data Services		1,575		1,575
Manitoba Forestry Resources		3,276		3,276
Manitoba Development Corp.		453	3,073	(2,620)
A.E. McKenzie		1,400		1,400
Paid in whole or in part from Departmental Appropriations				
Public Schools Finance Board:				
On Loans and Advances	1,670			
On School Debt	<u>18,863</u>	20,533		20,533
School Capital Financing Authority		17,269	18,998	(1,729)
Manitoba Health Services Commission -				
Hospital Debt		6,848		6,848
University of Manitoba		1,909	950	959
Manitoba Agricultural Credit		10,892	9,475	1,417
Manitoba Housing and Renewal Corp:				
Advances & Investments		2,474	1,944	
C.M.H.C.		20,600		21,130
Insurance Agency Operations:				
Manitoba Public Insurance Corp.			15,351	(15,351)
Workers' Compensation			13,986	(13,982)
Manitoba Crop Insurance Corp.			1,611	(1,611)
		<u>524,111</u>	<u>149,169</u>	<u>374,942</u>

NOTES:

1. The accounting policies for recording debt servicing cost may vary between the organizations shown above. EG. The Manitoba Telephone System and the Manitoba Hydro amortize debt expenses over the life of the issue whereas the Province writes off these expenses in the year of issue. Also, the Manitoba Telephone System provides an annual allowance for unrealized foreign exchange losses whereas the Province recognizes these losses when they are realized.
2. Approximately \$18,400,000 of the interest earnings shown for the School Capital Financing Authority was received from the Public Schools Finance Board.